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In the Supreme Court
OF THE
United States

OCTOBER TERM, 1977

No. 77-10

EXXON CORPORATION and
PHILLIPS PETROLEUM COMPANY,
Appellants,

vs.

GOVERNOR OF THE STATE OF MARYLAND, et al.,
Appellees.

On Appeal from the Court of Appeals of Maryland

MOTION FOR LEAVE TO FILE BRIEF OF AMICUS CURIAE
and
BRIEF OF AMICUS CURIAE IN SUPPORT OF APPELLANTS ON BEHALF OF PACIFIC LEGAL FOUNDATION

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The Pacific Legal Foundation respectfully requests leave to file the annexed brief *amicus curiae* in support of the appellants pursuant to this Court's Rule 42. Consent to the filing of the brief has been granted by all counsel for the appellants. Consent has been denied by counsel for the appellees. All responses have been lodged with the Court.

Pacific Legal Foundation is a nonprofit, tax-exempt corporation organized and existing under the laws of California for the purpose of engaging in litigation

in matters affecting the broad public interest. Policy for the Pacific Legal Foundation is set by a Board of Trustees composed of concerned citizens. Twelve of the seventeen-member Board are attorneys. The Board evaluates the merits of any contemplated legal action and authorizes such legal action only where the Foundation's position has broad support within the general community and is in the furtherance of the public interest. The Board of Trustees has approved the filing of the *amicus curiae* brief in this matter.

Pacific Legal Foundation requests permission to file an *amicus curiae* brief because it firmly believes that the decision of the Court of Appeals of Maryland upholding the Maryland divestiture law will have great adverse effect upon the general public, for as was found by the trial court, the law is "inversely related to the public welfare."

If that law stands, it will reduce competition resulting in increased prices for the consumer while at the same time limiting his selection and reducing the quality and quantity of services available. All marketers should have a right to participate in the retail marketing of petroleum products, for consumers are best served by a mix of all types of company and dealer operations. This the law prevents.

What is more disconcerting is the future utilization of the precedent that judicial approval of such a law will encourage. If the holding that the Maryland law is constitutional is allowed to stand, other states will be encouraged to enact similar petroleum divestiture laws, which actions will increase the adverse effect on consumers.

Even more alarming is the threat that approval of this law will constitute judicial sanction of divestiture laws in all industries that are now vertically integrated and those in which retailing is conducted by both company-operated and dealer outlets, some of which are automobile and truck dealers, fast-food restaurants, hotels and motels, and rental services. (United States Department of Commerce, Franchising In the Economy 1975-77, Tables 1-3.)

Divestiture laws constitute unreasonable state interferences with economic forces and an attempt to restructure our free enterprise system by restricting economic freedom without justification. They are totally in conflict with economic and free enterprise principles. Indeed, they would change the very nature of our free enterprise system. They would place a straightjacket on the rational utilization of investment capital.

The Maryland Court of Appeals' decision, in holding that the divestiture clause does not violate the Commerce Clause, is in conflict with the three-pronged balancing test established by this Court. *Pike v. Bruce Church,* 397 U.S. 137, 142 (1970), and recently reaffirmed in *A & P Tea Co. v. Cottrell,* 424 U.S. 366 (1976), and *Hughes v. Alexandria Scrap Corp.,* 426 U.S. 794 (1976).

When the law is measured by the *Pike* test it is found wanting, for:

1. The law furthers no legitimate local interest, rather it injures the general public;

2. The means utilized are totally irrational, for present federal and state laws achieve the desired ends without destructive inefficent divestiture; and

3. The Maryland divestiture law unduly and unjustifiably burdens interstate commerce by:

A. Restricting competition and injuring the consumer;

B. Disrupting the normal interstate flow of investment funds and petroleum;

C. Dislocating the intricate interstate petroleum refining and marketing system; and

D. Imposing artificial rigidity on the long established historic economic pattern of the petroleum industry, thus reducing free competition and economic freedom of choice.

The Maryland Court of Appeals' decision is in conflict with *Lawton v. Steele*, 152 U.S. 133 (1894), and *Goldblatt v. Town of Hempstead*, 369 U.S. 590 (1962), in that the divestiture law violates all the criteria established by those cases in that:

1. There is no menace to the general public which requires such a drastic dislocation of a legal business;

2. The law protects a special class of merchants to the detriment of the general public;

3. The means utilized are unreasonable, irrational, and unnecessary; and

4. The loss to the petroleum industry is disproportionate to any good to the public.

Pacific Legal Foundation respectfully submits that the magnitude of the adverse impact of this law upon the consumers of this nation will be tremendous and therefore respectfully requests permission to file the annexed *amicus curiae* brief so that the issues as they affect consumers may be fully and completely addressed.

Respectfully submitted,

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INTEREST OF AMICUS

The interest of *amicus* has been set forth in the preceding motion to file this brief.

OPINION BELOW

The opinion of the Court of Appeals of Maryland reversing the judgments of the Circuit Court for Anne Arundel County is officially reported at 279 Md. 410 (advance reports) and unofficially at 370 A.2d 1102 (advance reports). The supplemental opinion of

the Court of Appeals on motions for reconsideration and stay of judgment is officially reported at 279 Md. 456 (advance reports).

INTRODUCTION

The question presented in this case is whether or not Chapter 854, Laws of Maryland 1974, as amended by Chapter 608, Laws of Maryland 1975, and codified in the Maryland Annotated Code (1957), Art. 56, Section 157E (1972 Repl. Vol. 1976 Cum. Supp.), which will be henceforth referred to as the Maryland divestiture statute, is in conflict with the Commerce Clause of the United States Constitution in that:

1. It restricts free competition and injures the the consumers not only of the State of Maryland but of the United States;

2. It dislocates the intricate interstate petroleum financing, refining and marketing mechanisms to the detriment of the consumer; and

3. It imposes artificial rigidity on the historic economic pattern of the petroleum industry.

The divestiture law also is an unjustified utilization of the police power in that there is no evil to be corrected by it, rather it is legislation enacted to further the interests of a small special interest group to the detriment of society as a whole.

The Maryland divestiture law not only establishes a precedent for petroleum divestiture laws in other states, but also it will be interpreted as judicial approval of laws for divestiture of any vertically integrated company in any industry. Such a result will alter our entire free enterprise system to the detriment of the people of this nation.

ARGUMENT

I

THE MARYLAND DIVESTITURE LAW IS INVALID UNDER THE COMMERCE CLAUSE FOR IT UNDULY BURDENS AND DISRUPTS COMMERCE IN PETROLEUM AND INVESTMENT CAPITAL, IT SERVES NO USEFUL LEGITIMATE LOCAL INTEREST, AND IS IRRATIONAL AND NEEDLESSLY OPPRESSIVE

The Commerce Clause does more than confer on Congress the power to regulate commerce among the states. It creates an area of free trade and imposes limitations on the power of the states, by prohibiting them from unreasonably burdening or disrupting interstate commerce. *Boston Stock Exchange v. State Tax Commission,* ..... U.S. ....., 50 L. Ed. 2d 514, 523 (1977). Defining those limits has been the continuing responsibility of this Court. *Southern Pacific Co. v. Arizona,* 325 U.S. 761, 769 (1945). It is the task now before this Court.

The three-pronged balancing test applied in making that evaluation is well established by this Court's decisions. As was stated in *Pike v. Bruce Church,* 397 U.S. 137, 142 (1970), and recently reaffirmed in *A & P Tea Co. v. Cottrell,* 424 U.S. 366 (1976), and *Hughes v. Alexandria Scrap Corp.,* 426 U.S. 794 (1976):

> "Where the statute regulates evenhandedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits. Huron Cement Co. v. Detroit, 362 US 440, 443, 4 L Ed 2d 852, 856, 80 S Ct 813, 78 ALR2d 1294. If a legitimate local purpose is found, then the question becomes one of degree. And the extent of the burden that will be tolerated will of course depend on the nature of the local interest involved, and on whether it could be promoted as well with a lesser impact on interstate activities."

Less weight is given to the local interest in the balancing process when the law, as here, involves matters purely economic in nature and when they are closer to the concerns which the Commerce Clause committed to Congress, rather than to those concerning health, safety, or fraud. *H. P. Hood & Sons v. Du Mond,* 336 U.S. 525, 531 (1949); *Pike,* 397 U.S. at 143; *Huron Portland Cement Co. v. Detroit,* 362 U.S. 440, 442 (1960).

This "balancing test" presents three questions for this Court. They are:

1. Does the state law in its practical operation burden, restrict, or interfere with interstate commerce?

2. Does the state law further a legitimate local public interest?

3. If a legitimate local interest exists, but the law does burden interstate commerce, is that burden

excessive as compared with the putative local benefit? Or to rephrase the question, are the means reasonable for the accomplishment of the desired end or are there other less burdensome means?

We submit:

1. The law unduly burdens and disrupts interstate commerce;

2. The law furthers no legitimate local interest; rather, it promotes local special interests and injures the general public; and

3. The means utilized are totally irrational, for present federal and state laws achieve the desired ends without destructive, inefficient divestiture.

A. THE DIVESTITURE LAW UNDULY BURDENS AND DISRUPTS INTERSTATE COMMERCE

As all of the gasoline sold in Maryland is produced and refined in other states and shipped into Maryland, this law affects interstate commerce. *National Labor Relations Board v. Reliance Fuel Oil Corporation,* 371 U.S. 224 (1963). But more is involved than the flow of gasoline across state borders.

At the outset, we must ask what is commerce, for the Constitution does not define what is and what is not commerce among the states. This has been the responsibility of the courts. The courts have met that responsibility and have by their interpretation of that clause advanced the solidarity and prosperity of this nation. *Allenberg Cotton Co., Inc. v. Pittman,* 419 U.S. 20, 32. This Court is called upon to do so again in this

case, for if this Court does not act, the petroleum industry will be disastrously dislocated and the consumer will be seriously injured.

Certainly commerce, protected by our Constitution, is more than the physical transfer of tangible items in trade. Commerce to be meaningful must include every aspect of interstate manufacturing, transportation, marketing, and financing, for the Commerce Clause prohibits any action that, either on its face or in practical effect, unduly impedes the free flow of trade between states. This means any law that in "practical effect" restricts, limits, curtails the volume of, interferes with, adds extra costs to, impedes, slows down, discourages, or deters interstate commerce. Further, it prohibits state action that hampers the ability of interstate marketers to compete with local businesses, by way of regulations or financial impediments which affect those marketers' financial ability and efficiency to compete.

The Commerce Clause prohibits a state from taking action that will discriminate against interstate investors, producers, or distributors. It protects against any law which dislocates intricate interstate marketing mechanisms or imposes an artificial rigidity on the economic pattern of industry resulting in the reduction of free competition. *Hood*, 336 U.S. at 537; *Pike*, 397 U.S. at 146; *Allenberg Cotton Co., Inc.*, 419 U.S. at 29; and *Toomer v. Witsell*, 334 U.S. 385, 404 (1948).

Certainly such an interpretation and application is in accord with the purpose of the Commerce Clause.

That purpose is to create free trade among the states and prevent the states from unduly interfering with commerce between the people of the states. *A & P Tea Co.*, 424 U.S. at 377. The result envisioned is to guarantee free competition and thereby protect the consumer from exploitation. As was so well stated in *Hood*, 336 U.S. at 539:

> "Our system, fostered by the Commerce Clause, is that every farmer and every craftsman shall be encouraged to produce by the certainty that he will have free access to every market in the Nation, that no home embargoes will withhold his exports, and no foreign state will by customs duties or regulations exclude them. Likewise, *every consumer may look to the free competition from every producing area in the Nation to protect him from exploitation by any.* Such was the vision of the Founders; such has been the doctrine of this Court which has given it reality." (Emphasis added.)

Recently, this Court in *Hughes*, 426 U.S. at 806, after reviewing a number of cases in which it had been found that legislation violated the Commerce Clause, concluded:

> "The common thread of all these cases is that the State *interfered with the natural functioning of the interstate market* either through prohibition or through burdensome regulation." (Emphasis added.)

The Maryland divestiture law unduly and unjustifiably burdens interstate commerce by:

1. Restricting competition and injuring the consumer;

2. Dislocating the intricate interstate petroleum financing, refining, and marketing mechanism; and

3. Imposing artificial rigidity on the long established historic economic pattern of the petroleum industry.

1. The Law Restricts Free Competition and Injures the Consumer

As the purpose of the Commerce Clause is to guarantee free competition, and thereby protect the consumer from exploitation *(Hood, supra)*, the Maryland divestiture law is fatally defective for it destroys competition and exposes the consumer to exploitation. The trial court found:

> "[R]etail petroleum marketing in the State of Maryland is and has been a highly competitive industry." (E. 221.)[1]
>
> "Apart from restraining free competition, it was shown that divestiture would be harmful to competition in the industry, and would primarily serve to protect the independent dealers rather than the public at large. . . .
>
> "the court specifically finds that among the experts who testified there was unanimous agreement that in precluding the independent crude-deficient refiners from selling at retail in Maryland, a powerful source of price competition with the branded dealers would be eliminated, the effect of which would be anti-consumer, and that any law which had such effect would not be in the interest of the public at large. . . .

[1] "E." references as used herein are to the Joint Record Extract filed in the Court of Appeals of Maryland.

> "The court also finds from the preponderance of the evidence that the law will preclude all of some thirty-two producer-refiners not now in the State from ever entering the competitive market in Maryland, and vertical integration will be prohibited. Neither effect is in th [*sic*] public interest since competition is essentially for consumer benefit." (E. 243.)
>
> "The court finds that . . . apart from there not being demonstrated a real and substantial relation to the object sought to be attained by the means selected, the evidence presented before it indicates that the statute is inversely related to the public welfare." (E. 244.)

The recognized experts who testified for the plaintiffs stated the law will reduce competition in the retail market, will increase the price of petroleum products, will reduce services to the consumer such as the quality and number of products available; the reliability of products and services; the range of prices; cleanliness of stations and station employees; speed of driveway service; innovations in service; product development; and merchandising methods.[2]

Even the state's only expert witness, Dr. James M. Patterson, was of the opinion that the law would reduce competition and services available to the public for there are advantages to the public by allowing

[2] Theodore Levitt, Professor of Business Administration, Harvard University, E. 395-96, 400, 402-04. Dr. Charles H. Berry, Professor of Economics and Public Affairs of Princeton University, E. 437-38, 445-46. Dr. Matityahu Marcus, Professor of Economics, Rutgers University, E. 468-70, 472. John H. Lichtblau, Economic Researcher and Executive Director of Petroleum Industry Research Foundation, E. 508-10.

company-operated stations. (E. 555, 569-70, 573, 581, 584.)

As the trial court found and the state's only expert witness, Dr. Patterson, admitted: (1) independent refiner-marketers, such as Ashland, are procompetitive, yet the law will remove them from the market (E. 235); (2) the law is not consistent with sound economic principles in that it requires Hudson Oil to give up Maryland retail stations once it has built its refinery (E. 236); and (3) the law has negative aspects with respect to Commonwealth-PMC (E. 236).

Perhaps the full impact of the law on competition and price can be better appreciated when put in more specific terms. Eighteen interstate producers or refiners have 209[5] company-operated retail service stations in Maryland. (E. 70-71.) These stations must be divested either by sale or lease to independent dealers. Some companies will be forced to abandon the Maryland market. (E. 360, 388-89, 457, 492.) The ouster of this many competitors from the retail market will deprive consumers of the benefit of free competition, and is, standing alone, a violation of the Commerce Clause.

More than that the nature of the businesses being driven from the competitive market shows that divestiture will injure competition.

[5]According to the records of the Gasoline Tax Division of the Comptroller's Office, there were a total of 3,757 retail gasoline service station dealers in the State of Maryland as of July 1, 1974. For some brands of gasoline sold there were no figures available as to the number of stations marketing them. (E. 71.) The Court stated 229 retail stations would be subject to divestiture. (E. 244.)

The burden of the statute falls most heavily on independent refiners and "nonmajor" oil companies, for the majority of "major brand" stations are presently operated by independent dealers. (E. 70-71.) Most of the refiner or producer company-operated stations in Maryland are "private brand" stations (E. 69-71, 397), indeed these stations constitute the majority of "private brand" stations in Maryland. (E. 221, 383, 453, 456, 488-89, 492, 499.) The trial court found that most "private brand" stations generally emphasize price and sell at lower prices than most independent dealer-operated stations. (E. 221.)

These "private brand" stations must be company operated to survive. Such nonrecognized brands must retail their products at prices lower than those at which advertised brands are sold. (E. 488-89.) To sell gasoline at a lower price, "private brand" operations must maintain high throughput and low overhead. (E. 454, 457-58, 507.) These objectives are achieved by small investment in the property, no advertising, no service facilities and no automotive maintenance and repair services, no credit cards, long hours of operation—typically 18 hours a day, 365 days a year—few employees, and a skeletal administrative force. (E. 382-87, 455, 491.) It is the experience of Kayo, PMC, Ashland, and Hudson Oil Company (Hudson) that the maintenance of low overhead, low-priced image, long hours, and competitive prices requires tight control of the station's day-to-day operations which would be legally and practically impossible with independent dealers. (E. 388, 453, 456, 489, 492, 499.)

The inability to operate "private brand" stations on other than a company-operated basis is evidenced by the fact that most "private brand" marketers, including some that have experimented with dealer operations, use company operations to the total exclusion of dealer operations. That is true for Kayo, PMC, and Ashland, as well as for Hudson. (E. 381, 453, 488-89, 499.) Dealer operations have been tried by "private brand" marketers and they have been unsuccessful. (E. 453, 488-89, 499.) When Hudson experimented with dealer stations which involved about 30 of its then 120 stations, it "completely lost control of [its] stations. We had dirty stations. The dealer would not carry out the orders, and of course we did not and were not able to enforce certain regulations because they were leased out; and we cancelled our leases and took the stations back over." (E. 499, 502.) In addition, the lack of service facilities and the high cost of gasoline makes PMC's operations unattractive to dealers. (E. 456-68.)

As the divestiture law will drive these price-competitive stations from the market it will limit competition and result in increased costs to the consumer.

In addition to forcing the withdrawal of present competitors, the law precludes 32 producers or refiners, not currently distributing their products in the Maryland market, from entering that market. (E. 243.) These companies utilize aggressive pricing strategies. (E. 401.) This will further restrict competition to the detriment of the general public.

Abandonment of operations by at least some of the present competitors in the Maryland retail gasoline

market would also affect supplies at the wholesale level. For example, Ashland is an important factor in the Maryland wholesale gasoline market. (E. 494, 577.) It would be extremely difficult for the company to remain in Maryland as a wholesaler if it lost its retail outlets. The likely result would be diversion of its activities into other states. (E. 493.) Such a result would injure the public by reducing supplies available to independent gasoline marketers and weaken that segment of the retail market which sells gasoline at discount prices. (E. 577.)

If the marketplace is to behave competitively, it must have many competitors. This law achieves the opposite result, for it removes aggressive price competitors from the marketplace, depriving the public of the benefits of competition and lower prices. This is clearly a violation of the Commerce Clause, for it defeats the purpose of that clause as envisioned by our founding fathers and given life by our courts. The divestiture law is thus invalid.

2. The Law Disrupts the Normal Interstate Flow of Both Investment Funds and Petroleum and Dislocates the Intricate Interstate Petroleum Refining and Marketing System

A state law which interferes with the natural functions of the interstate market, *Hughes, supra,* or dislocates the intricate interstate marketing mechanism, *Allenberg Cotton Co., Inc.,* 419 U.S. at 29, violates the Commerce Clause.

The Maryland law causes such disruption. It destroys an established retail marketing structure. It prohibits entry into marketing by new competitors, if

they are producers or refiners. It disrupts the wholesale market by prohibiting backward integration. It prohibits natural growth, with resulting cost reductions. It discourages the flow of investment capital into Maryland and into the stocks of affected companies for it causes substantial capital loss through forced sales, and reduces profits by eliminating an entire operating segment of the affected industries, their retailing branches; this in turn adversely affects the economic stability of those companies and discourages the flow of investment capital into them.

To appreciate this disruption an overview of the petroleum industry will be helpful for the marketing of petroleum products in Maryland is part of an intricate and complex national, indeed international, financial and marketing mechanism. A dislocation of that system by one state will adversely affect the consumers, not only in that state, but in all the other states, for it will adversely affect production, refining, distribution, and investment.

In the United States there are some 15,000 independent crude oil producers; 110 small refiners and 30 major refiners (some of which are also crude producers); 598 importers (other than refiners) of both crude and refined products; 200 gathering systems between crude producers and refiners (pipelines, etc.); 26,000 wholesalers; and 268,000 retailers.[4] This totals to more than 300,000 firms which perform the following functions:

[4]Federal Energy Administration Regulation—Report of the Presidential Task Force, 1977, p. 40.

1. exploration and production of crude oil;
2. gathering and purchasing of crude;
3. transportation of crude to refineries;
4. refining;
5. marketing, both wholesale and retail; and
6. research and development.

Firms operating in the petroleum industry are of greatly varying sizes. At one end are the fifteen to twenty-five major integrated petroleum companies, such as Exxon, which engage in all functions performed by the industry. At the other end are the many thousands of independent companies whose activities are confined to just one activity within the industry.

In the petroleum industry there has been a historical pattern of vertical integration, both forward and backward, for very sound economic reasons. Integration of operations (production of crude, refining, and marketing) provides genuine economic efficiencies with savings passed on to the consumer. The record establishes this and the compelling reasons for it.

With this overview in mind, we can now more fully appreciate the disruption to this intricate marketing system that divestiture will cause.

In evaluating this disruption one fact is paramount; that disruption will adversely affect interstate commerce—for Maryland has no producers of crude nor has it any refineries. All petroleum products marketed in Maryland are produced and refined elsewhere and

shipped into Maryland. (E. 186.) Thus, there will be a shift from the normal flow of petroleum products to Maryland and a disruption of interstate commerce. (E. 405.)

Retail Market System

If this law stands, 209 outlets now in operation will be divested. (E. 388-89, 456-57, 460, 492.) The disruption that will result is obvious.

Wholesale Market System

Forced abandonment of operations by at least some of the present competitors in the Maryland retail gasoline market would also affect supplies at the wholesale level. For example, Ashland is an important factor in the Maryland wholesale gasoline market. (E. 494, 577.) It would be extremely difficult for the company to remain in Maryland as a wholesaler if it lost its retail outlets. The likely result would be diversion of its activities into other states. (E. 493.) This will disrupt the marketing system and have interstate impact.

Refining System

Under the law, no gasoline retailer now operating will be allowed to integrate backwards to either refining or production. (E. 438.)

Historically such backward integration has been the traditional growth pattern in petroleum marketing as evidenced by the growth of Exxon and many other companies. (E. 402-03.) This pattern is continuing to evolve today, as demonstrated by Hudson. Hudson has approximately 315 retail outlets in 36 states, including five stations in Maryland. All are

company operated. (E. 498.) Recently Hudson decided to construct a refinery to provide the company with its own source of refined products. (E. 499-500.) When the refinery comes "on stream," Hudson's competitive posture improves, but this law will force the company to divest itself of its retail outlets. (E. 500.) The state's only expert witness concedes this would be detrimental to the Maryland consumer. (E. 584.)

Not only will the law prevent backward integration, it will disrupt refining operations.

Because of the capital intensive nature of a refinery operation, it is necessary from an economic standpoint to have the refinery operating at peak levels. (E. 487-91.) This is accomplished in part through an assured marketing arm for the refined products. (E. 509.) For oil companies such as Exxon, Shell, and Gulf, which market largely through independent dealers, the dealers serve as the principal outlet for gasoline from the refineries. For companies such as Commonwealth and Ashland, which market "private brand" gasoline through company-operated stations, the stations serve as assured outlets. (E. 489-91.) The uncontroverted testimony shows that the presence of company-operated stations has enabled Ashland to insulate itself from the loss of substantial volumes of uncontrolled business and to remain an effective competitor. (E. 490-91, 509.) The act, by stripping the integrated companies of their regular market, will dislocate their refining operations and thereby disrupt the complex refining and marketing system.

Investment Market

Another aspect of interstate commerce which cannot be overlooked is that of interstate investment. The act will cause dislocation in the petroleum capital market. It will create positive disincentives for certain firms to invest capital and do business in Maryland. (E. 405.) Certainly the flow of investment capital is essential to interstate commerce and its flow in the normal channels of commerce is as protected as that of any product.

There are 32 integrated refiner-marketers of gasoline, who are multi-state retail operators, but are not now in Maryland retailing. They are potential entrants into the Maryland market, but the law denies them entry. These companies utilize aggressive pricing strategies. (E. 401.) In order to make such entry they must be able to maintain low prices and tight operating control over their stations. Long operating hours are needed to build the necessary volume and goodwill to make operations profitable. This cannot be achieved with independent dealers. (E. 401, 438, 491-92.) Their exclusion affects the flow of investment capital in interstate commerce.

There is further economic impact that will result in dislocation of the interstate refining and marketing system.

1. Producers and refiners will be denied profits from direct retailing of petroleum products. (E. 358.)

2. Producers and refiners will have to divest themselves of substantial capital investment in Maryland, probably at substantial financial loss. (E. 244.)

These losses will impact the availability of investment capital for all such vertically integrated companies, for such investment will be far less desirable. This will have a chilling effect not only on interstate commerce, but upon our entire national economy, for restrictions on the mobility of capital cannot have a good effect—only bad. This in and of itself is in violation of the Commerce Clause.

This law's ultimate effect on the intricate petroleum mechanism may prove to be even greater, for if it stands, it will afford a precedent and authority for petroleum divestiture laws in other states. Such laws will magnify the disruptive effect detailed above. The end result will be disastrous to the companies involved and to the public.

Even more alarming is the threat that judicial approval of this law will constitute judicial precedent for divestiture laws affecting all industries that are now vertically integrated and those in which retailing is conducted by both company-operated and dealer outlets, some of which industries are automobile and truck dealers, fast-food restaurants, hotels and motels, rental services for automobiles, trucks, and equipment, nonfood retailing, and softdrink bottling. (United States Department of Commerce, Franchising In the Economy 1975-77, Tables 1-3.)

If the Maryland law is a valid exercise of state power, then that power extends to all vertically integrated industries. Such law will change the basic structure of American business to the detriment of the public.

As this law disrupts the normal interstate flow of investment funds and petroleum and dislocates the intricate interstate petroleum refining and marketing system, it violates the Commerce Clause.

3. The Law Imposes an Artificial Rigidity on the Long Established Historic Economic Pattern of the Petroleum Industry which Results in the Reduction of Free Competition

This Court has held that if "the necessary tendency of the statute is to impose an artificial rigidity on the economic pattern of industry" in interstate commerce, it violates the Commerce Clause. *Hood, supra; Pike,* 397 U.S. at 146; *Toomer,* 334 U.S. at 404.

The Maryland divestiture law violates this prohibition for it artificially and unreasonably restructures the petroleum industry (E. 482) in a manner which is contrary to the economic forces which mandated the historic development of gasoline marketing into its present vertically integrated structure.

The law achieves this by dictating that all retailing of petroleum products must be done through independent dealers. History teaches that this is often unworkable and economically disastrous for the petroleum industry and ultimately for the consumers.

We have already treated in detail the intricate nature of the petroleum industry and its historical evolution and the economic reasons for this natural trend to vertically integrate. We shall not prolong this petition by doing so again in detail.

Indeed such a detailed analysis is unnecessary for it is patent that the law will restructure the petroleum industry as follows:

1. The law forces producers and refiners to divest themselves of established retail outlets, thus it restructures their long established business structure, it drastically alters their method of conducting business and it artificially dictates limits to areas of investment. It flies in the face of the historical development of the petroleum industry. It strips business of its right to economic choice.

2. The law closes the Maryland retail market to refiners and producers who have not as yet entered the retail market, but may at a future date desire to do so. Such restriction constitutes unjustified limitations on normal business expansion and progress.

3. The law prohibits retailers from integrating backwards into refining or producing, or in the alternative drives them out of the retail market in which they now function. Thus the law prevents normal economic growth. (E. 457.)

Very simply the law improperly imposes "a straightjacket on the appellee company with respect to the allocation of its interstate resources." *Pike,* 397 U.S. at 146.

Since the law imposes an irrational rigidity on the long established economic pattern of the petroleum industry it violates the Commerce Clause.

B. THERE IS NO LEGITIMATE LOCAL PUBLIC INTEREST SERVED BY THIS LAW; INDEED, IT INJURES THE PUBLIC WELFARE

The law serves no legitimate local purpose, for it is designed to protect limited special interests; thus it violates the Commerce Clause for it adversely impacts interstate commerce.

Although the state may shelter its people from menaces to their health or safety and from fraud, it lacks the power to retard, burden, or constrict the flow of interstate commerce for the economic advantage of a small class of its citizens. *Polar Ice Cream & C. Co. v. Andrews,* 375 U.S. 361 (1964); *General Motors Corp. v. Washington,* 377 U.S. 436, 462 (1964); *Baldwin v. Seelig,* 294 U.S. 511, 523 (1935).

In *Hood,* 336 U.S. at 542, the state denied a license for a new plant. Among the reasons were the increase in competition by diverting supplies of milk from other plants in the area and a tendency to deprive local markets of needed supplies during the short season. This Court recognized that to do so would exclude an entirely new foreign handler from coming into the state to purchase. This Court then held:

> "But here the challenge is only to a denial of facilities for interstate commerce upon the sole and specific grounds that it will subject others to competition and take supplies needed locally, an end, as we have shown, always held to be precluded by the Commerce Clause."

In the present case the trial court found:

> "In all the more than one hundred eighty-five pounds of pleadings, motions, briefs, exhibits and depositions before this court, there is no concrete evidence that the act was justified as to the classes of operators singled out to be affected in order to promote the general welfare of the citizens of the State. Rather, it is apparent that the entire bill is designed to benefit one class of merchants to the detriment of another." (E. 244.)

The trial court further found that the statute did not benefit the public, but more, from the evidence presented, it found that "the statute is inversely related to the public welfare." (E. 244.)

The state's own witnesses conceded that the statistics compiled for the Gasoline Tax Division's Report, which allegedly formed the basis for the legislation, established neither a relationship between the survey results and the law, nor a necessity which would justify the act. The chief of the state's Gasoline Tax Division stated he had no evidence of any major oil company having misallocated among dealer-operated and company-operated stations, and that a state audit of Exxon and a consultation with Getty disclosed fair allocation. (E. 523, 527, 534, 540, 547.)

As previously set forth in detail, the law is destructive of competition, will injure the general public by limiting choice and services while at the same time increasing prices. Its sole purpose is to protect a small special interest class. This brings the law into conflict with the Commerce Clause.

C. THE LOCAL INTEREST CAN BE BETTER SERVED BY OTHER MEANS ALREADY AVAILABLE AND FAR BETTER DESIGNED TO ACHIEVE THE DESIRED END

The supposed purpose of the legislature in enacting this law was to promote and protect vigorous free competition by mandating that producers and refiners divest themselves of company-operated stations and that all retail outlets be operated by independent dealers. We have previously established that the law

will achieve exactly the opposite result. It will decrease competition to the detriment of the consumers.

Here we are concerned with the question of whether or not there are more adequate and less burdensome alternatives, for the Commerce Clause is violated if the burden imposed on interstate commerce is clearly excessive in relation to the putative local benefits. *Pike,* 397 U.S. at 137. In making such a determination, one of the questions is whether adequate and less burdensome alternatives exist. *A & P Tea Co.,* 424 U.S. at 373. This in turn includes a determination of whether this law bears a real and substantial relationship to the object sought to be obtained and whether or not it is excessive in scope in its attempt to solve the problems.

Potentially, divestiture is a drastic and extreme means to achieve any local end.

In the case of this law, producer-refiners are required to divest themselves of 229 outlets amounting in value to over $12,800,000. The trial court observed, "there was no suggested way in which those affected could obtain a fair market price in arms-length transactions when the potential purchasers were well aware of the exigencies of the occasion. The result would amount to forced sales or leases on a buyers' market, with scant chance of obtaining a fair return on investments made in Maryland in good faith by the entities affected." (E. 244.)

There is no question that adequate and less burdensome alternatives already exist. The trial court found:

> "There was no proven detrimental effect upon the retail market caused by company-owned-and operated stations which could not be curbed by federal and state anti-trust laws." (E. 243.)

Indeed the state's only expert, Dr. Patterson, was of such a view, for the trial court cited Dr. Patterson's admission that he "was of the opinion that the scope of the law was overly broad." (E. 243.)

An appreciation of the extent to which present laws, both state and federal, better achieve the purported purpose of the divestiture statute without resorting to its destructive and irrational means is best achieved by separately evaluating each of the so-called problem areas separately.

1. Preservation of the Retail Dealers as Independent Businessmen, by Eliminating Unfair and Arbitrary Cancellations of Retail Contracts by the Vertically Integrated Markets, is Assured by Federal and State Laws

One of the state's contentions is that the act is necessary to preserve the retail dealer as an independent businessman and eliminate the takeover of dealer stations by vertically integrated producers and refiners. (E. 277.) This end is already assured by federal and state laws.

At the federal level, the Sherman Antitrust Act outlaws conspiracy in restraint of trade (15 U.S.C. § 1) and prohibits cancellation of retail contracts where the purpose is to create or maintain monopoly power (15 U.S.C. § 2).

Section 5 of the Federal Trade Commission Act (15 U.S.C. § 45(a)(1)) proscribes "unfair methods

of competition and unfair or deceptive acts or practices in or affecting interstate commerce." This Act has been applied to unfair and arbitrary cancellations of retail service station leases as well as unfair lease provisions and coercive purchase requirements even though antitrust laws were not shown to be violated.

At the state level, the Maryland Gasoline Products Marketing Act, the Maryland "Dealer Day in Court" statute (Comm. L. Art. §§ 11-301, *et seq.*, Md. Anno. Code), extensively regulates all marketing agreements between petroleum distributors and dealers and expressly provides civil remedies both in the case of an illegal termination or cancellation of a marketing agreement and in the case of an unreasonable refusal to renew such an agreement.

These federal and state laws are far better designed to prevent the evil envisioned by the legislature than is divestiture. Even more they protect the public by assuring vigorous competition with resulting price reduction and an increase in available service and selection.

2. The Prevention of Retail Price Maintenance Schemes, Price Discrimination, or Predatory Pricing Thereby Ensuring Lower Prices for Consumers is Assured by Federal and State Laws

Another supposed evil the divestiture law is to protect against is price discrimination or predatory pricing which affects competition at the retail or any other level of the distribution system and the coercion of dealers to participate in retail price schemes.

At the federal level the Sherman Antitrust Act, 15 U.S.C. §§ 1, *et seq.*, the Clayton and the Robinson-Patman Act (15 U.S.C. §§ 13, *et seq.)* are designed to prevent price discrimination and predatory pricing.

On the state level, Maryland has enacted three statutes which prohibit anticompetitive pricing practices. The Maryland Antitrust Act complements the federal antitrust statutes. (Comm. L. Art. §§ 11-201, *et seq.*, Md. Anno. Code.) The Maryland Unfair Sales Act (Comm. L. Art. §§ 11-401, *et seq.*, Md. Anno. Code), protects the competitive independence of the retail marketer by not permitting the distributor to prescribe in any way the retail price of the product (*e.g.*, motor gasoline). The Maryland Gasoline Products Marketing Act (Comm. L. Art. § 11-304(c), Md. Anno. Code) prohibits price setting by distributors.

Thus, both federal and state laws achieve the protection from price controls far more effectively and equitably than does divestiture.

3. Federal and State Laws Ensure the Uniform Allocation of Gasoline Among All Dealers in Periods of Shortage

Another proposed justification for the divestiture law was the belief that producer-refiners in periods of shortages, such as the period of the OPEC oil embargo of 1973, favored the stations operated by themselves, and the fear that in future shortages they would again do so. Factually, there was no evidentiary support for this reasoning.

A state witness testified there was no evidence that a major oil company had misallocated. (E. 233.)

Indeed the state's survey of Exxon established that it had allocated fairly. (E. 232.)

Regardless of that, at the federal level, the Federal Emergency Petroleum Allocation Act of 1973 (15 U.S.C. §§ 751, *et seq.*), amended and extended by the Energy Policy and Conservation Act (Pub. L. No. 94-163 (1975)), and regulations promulgated thereunder (10 C.F.R. §§ 210-213) ensure that during times of shortage of motor gasoline, there shall be equitable distribution of supplies to meet regional needs and to preserve competition in the marketplace.

At the state level Paragraph F of the Maryland divestiture statute (56 Md. Anno. Code 157F) also provides for uniform and equitable allocations in "periods of shortage."

This summary review of federal and state law establishes that present laws are far better designed to achieve the ends which purportedly prompted the Maryland divestiture law without the drastic and unjustified hardship caused by that law.

II

THE MARYLAND DIVESTITURE STATUTE VIOLATES THE DUE PROCESS MANDATE OF THE FEDERAL CONSTITUTION IN THAT IT BEARS NO REAL AND SUBSTANTIAL RELATIONSHIP TO THE PUBLIC HEALTH, WELFARE, SAFETY, OR MORALS AND THEREFORE CONSTITUTES AN ARBITRARY AND CAPRICIOUS EXERCISE OF THE POLICE POWER

When it is shown that state action threatens significantly to impinge upon constitutionally protected freedom it becomes the duty of the court to determine whether the action bears a reasonable relationship to the achievement of the governmental purpose asserted as its justification. *Bates v. Little Rock,* 361 U.S. 516, 525 (1960).

The classic statement of the law is set forth in *Lawton v. Steele,* 152 U.S. 133, 137 (1894). After recognizing that great discretion is vested in the legislature to determine not only what the interests of the public require, but what measures are necessary for the protection of such interests, this Court nevertheless held that such discretion is subject to judicial review and set down the standard for such review, to wit:

> "To justify the state in thus interposing its authority in behalf of the public, it must appear, first, that the interests of the public generally, as distinguished from those of a particular class, require such interference; and, second, that the means are reasonably necessary for the accomplishment of the purpose, and not unduly oppressive upon individuals. The legislature may not, under the guise of protecting the public interests, arbitrarily interfere with private business, or impose unusual and unnecessary restrictions upon lawful occupations. In other words, its determination as to what is a proper exercise of its police powers is not final or conclusive, but is subject to the supervision of the courts."

In *Goldblatt v. Town of Hempstead,* 369 U.S. 590, 595 (1962), the Court summarized the information needed to evaluate a law's reasonableness as follows:

> "To evaluate its reasonableness we therefore need to know such things as the *nature of the menace*

against which it will protect, the *availability and effectiveness of other less drastic* protective steps, and the *loss which appellants* will suffer from the imposition of the ordinance." (Emphasis added.)

The Maryland divestiture law violates all of these criteria for:

1. There is no menace to the general public which requires such a drastic dislocation of a legal business;

2. The law protects a special class of merchants to the detriment of the general public;

3. The means utilized are unreasonable, irrational, and unnecessary; and

4. The loss to the petroleum industry is disproportionate to any good to the public.

A. THERE IS NO MENACE TO THE GENERAL PUBLIC WHICH REQUIRES SUCH DRASTIC DISLOCATION OF LEGAL BUSINESS

To evaluate interest of the public we must first determine if there is in fact a menace to the general public.

The trial court found:

> "The Attorney General in his opening statement maintained that there was an evil at hand identified by the Legislature. Presumably, he referred to a contrived shortage of petroleum and heating oils, since this was the topic of the Governor's inquiry. He stated that his witnesses would show that divestiture would restore and maintain free competition; that the law was aimed at preserving competition and not to protect any identifiable group; that company-owned

> and operated stations produced detrimental effects upon the retail market of petroleum products.
>
> "The evidence did not support these statements. The court finds from all the evidence produced before it that the shortage was actual and beyond the control of the legislature of the State or of the Congress of the United States and was directly related to the OPEC embargo. Defendants' witness, Dr. Patterson, admitted that even he was of the opinion that the scope of the law was overly broad. Apart from restraining free competition, it was shown that divestiture would be harmful to competition in the industry, and would primarily serve to protect the independent dealers rather than the public at large. There was no proven detrimental effect upon the retail market caused by company-owned-and operated stations which could not be curbed by federal and state anti-trust laws." (E. 242-43.)

We have in our Commerce Clause argument set forth in detail the evidence which supports this finding by the trial court and establishes there was no evil crying out for cure.

B. THE STATUTE DOES NOT BENEFIT THE PUBLIC GENERALLY BUT RATHER A PARTICULAR GROUP OF BUSINESSMEN

The trial court found:

> "there is no concrete evidence that the act was justified as to the classes of operators singled out to be affected in order to promote the general welfare of the citizens of the State. Rather, it is apparent that the entire bill is designed to benefit one class of merchants to the detriment of another." (E. 244.)

The trial court further found that the law was inversely related to the public welfare. (E. 244.)

As shown under our Commerce Clause argument the evidence established that the law would reduce competition and benefit one class, the independent dealers. This is crass special interest legislation and therefore an abuse of the state's police powers.

C. THE MEANS ARE UNREASONABLY IRRATIONAL AND UNNECESSARY FOR THE ACCOMPLISHMENT OF THE PURPOSE

The Attorney General claimed that the divestiture law was necessary to restore and maintain free competition and prevent detrimental effects upon retail marketing resulting from operation of stations by companies that were also producers and refiners.

The trial court found:

> "Retail petroleum marketing in the State of Maryland is and has been a highly competitive industry." (E. 221.)

The evidence set forth previously establishes that the law will in fact decrease competition and increase prices.

More specifically, as already shown, numerous federal and state laws presently exist which are far better designed to correct any problems. But, more important, these laws achieve that end in a rational manner. This law does not.

D. THE MEANS ARE UNDULY OPPRESSIVE UPON INDIVIDUALS

Finally the question is what loss will the affected companies suffer as a result of the divestiture legislation?

The trial court found:

> "Turning the Lawton's other tests—that the means employed must be reasonable, not unduly oppressive or beyond the necessities of the case—it will be observed that the means of carrying the law into effect as to the producer-refiners would have necessitated that on or before July 5, 1975 some 229 outlets amounting in value to over $12,800,000.00 would have to have been divested, unless the Comptroller were to be convinced of the merits of extending the divestiture period. There was no suggested way in which those affected could obtain a fair market price in arms-length transactions when the potential purchasers were well aware of the exigencies of the occasion. The result would amount to forced sales or leases on a buyers' market, with scant chance of obtaining a fair return on investments made in Maryland in good faith by the entities affected.
>
> "This court has been referred to no situation short of the Prohibition Era where any group of retailers engaged in lawful mercantile activity have been compelled to divest without at least an appreciable period designed to afford amortization of the assets affected by the order. It finds the means unduly oppressive and beyond the necessities of the case." (E. 244.)

Divestiture is an extreme measure. Its disruptive impact on the retail and wholesale market, refining and investment has already been set forth in detail. The losses to the companies affected are so great as to be confiscatory. The artificial rigidity on business is absolutely unprecedented and unjustified. In total

the loss is great; the benefit to the public non-existent.

The Maryland divestiture legislation, under the guise of protecting the public interest, arbitrarily interferes with a legitimate private business and imposes unusual and unnecessary restraints upon lawful occupations. It is therefore an unlawful exercise of the state's powers.

CONCLUSION

As the Maryland divestiture law violates the Commerce Clause of the United States Constitution and is an unauthorized exercise of the police powers of the state, it is respectfully requested that this Court note probable jurisdiction and find this law to be unconstitutional.

Respectfully submitted,

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